The Commonwealth of Massachusetts

DEPARTMENT OF
TELECOMMUNICATIONS AND ENERGY

D.T.E. 04-35 October 28, 2004

Investigation by the Department of Telecommunications and Energy pursuant to G.L. c. 164, § 94A into the Petition of The Berkshire Gas Company for approval of a Gas Sales Agreement with Nexen Marketing and an Agency Agreement and a Management Services Agreement with Northeast Gas Markets LLC.

APPEARANCES: James M. Avery, Esq.
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FOR: THE BERKSHIRE GAS COMPANY
Petitioner

I. INTRODUCTION

______On March 18, 2004, The Berkshire Gas Company ("Berkshire" or "Company"), pursuant to G.L. c. 164, § 94A, submitted for approval by the Department of Telecommunications and Energy ("Department") (i) a gas sales agreement ("Sales Agreement") that the Company executed with Nexen Marketing ("Nexen") and (ii) an agency agreement ("Agency Agreement") and a management services agreement ("Management Services Agreement") that the Company executed with Northeast Gas Markets LLC ("NEGM").[1] The Sales Agreement replaces a supply contract between Berkshire and EnCana Corporation ("EnCana").[2] The Agency and Management Services Agreements require NEGM to perform day-to-day administrative services for Berkshire related to the Sales Agreement. The petition was docketed as D.T.E. 04-35.

On April 15, 2004, pursuant to notice duly issued, the Department conducted a public hearing to afford interested persons the opportunity to comment on Berkshire's proposal. No members of the public were in attendance. An evidentiary hearing was held at the Department's offices on May 17, 2004. Berkshire presented the testimony of William L. Barschdorf, supervisor of gas supply support for the Company. The evidentiary record includes 19 exhibits.

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1 NEGM is a project development and gas supply contract management firm located in Beverly, Massachusetts. NEGM was originally formed in 1979 to support the interest of a consortium of local distribution companies in obtaining incremental gas supply and associated transportation capacity (Exh. BG-1, at 4).

2 The EnCana contract was approved by the Department in The Berkshire Gas Company, D.T.E. 02-56 (2002).

II. DESCRIPTION OF PROPOSED AGREEMENTS

A. Sales Agreement

The Sales Agreement is the result of a competitive solicitation pursued by Berkshire and several other local distribution companies ("LDCs") in the northeast on a coordinated basis (collectively, the "Working Group")[3] to replace the Company's supply contract with EnCana dated August 7, 2002, which expired on March 31, 2004 (Exh. BG-1, at 3).[4] The Sales Agreement entitles Berkshire to receive, on a firm basis, 1,080 dekatherms ("Dth") per day from Nexen to be delivered at the international boundary near Niagara Falls where the facilities of Tennessee Gas Pipeline Company ("TGP") and TransCanada Pipelines Limited interconnect (id. at 13). The Sales Agreement is for a term of three years (id.).

The Sales Agreement includes pricing provisions of gas deliveries which are based on an indexed price as published monthly in Platts Inside FERC's Gas Market Report for deliveries at Niagara, New York (id.). Berkshire maintains that the Sales Agreement is consistent with the Company's portfolio objectives established in its most recent forecast and requirements plan approved by the Department, and contributes to the Company's overall goal

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[3] The other local LDCs include Bay State Gas Company; Boston Gas Company d/b/a KeySpan Energy Delivery New England; The Brooklyn Union Gas Company d/b/a KeySpan Energy Delivery New York; Energy North Natural Gas, Inc. d/b/a KeySpan Energy Delivery New England; Essex Gas Company d/b/a KeySpan Energy Delivery New England; KeySpan Gas East Corporation d/b/a KeySpan Energy Delivery Long Island; and Northern Utilities, Inc. (Exh. BK-3, at 1).

[4] Berkshire has entered into a short-term, interim agreement with Nexen for gas purchases pending Department approval of the Sales Agreement (Exh. BK-23, at 1).

of maintaining a diversified supply mix with reliable, competitively priced gas supply (id. at 13-14).

The Company explained that the Sales Agreement provides benefits to its customers (id. at 14). First, the inclusion of a Canadian resource in its resource portfolio helps the Company diversify its pipeline base-load supply (id.). Second, the competitive solicitation pursued by the Working Group allowed Berkshire to secure a least-cost replacement supply with attractive pricing provisions and flexible contract terms, compared to what it would have obtained on a stand-alone basis (id.).

B. Agency Agreement

Under the Agency Agreement[5], NEGM will act on Berkshire's behalf as the administrative agent for all purposes under and with respect to the Sales Agreement (Exhs. BG-1, at 15; BG-4, at 1). The functions that NEGM shall perform under the Agency Agreement include the following: (1) submit nominations to Nexen; (2) receive invoices and make payments on behalf of Berkshire; (3) declare, or receive notice of, force majeure on behalf of Berkshire; and (4) execute all other necessary actions related to the Sales Agreement, including the preparation and filing of U.S. Customs Department forms and payments and other operational reports as may be required by relevant regulatory agencies (Exh. BG-1, at 15).

[5] The other members of the Working Group also are parties to the Agency Agreement, receiving the same services from NEGM for their respective sales agreements (Exh. BG-3, at 1).

The Agency Agreement is coterminous with the Sales Agreement (Exh. BG-4, at 7). However, Berkshire has the right to terminate the Agency Agreement under specified conditions (id.). The Agency Agreement can also be renewed (id. at 6-7).

C. Management Services Agreement

Under the Management Services Agreement[6], NEGM will provide operational, management, contract administration, coordination, reporting and accounting services for the administration of the Sales Agreement (id. at 2). The functions that NEGM shall perform under the Management Services Agreement include, among others, the following: (1) receive notices from Berkshire of its scheduled contract quantities pursuant to the Sales Agreement; (2) transmit to Berkshire all notices received from Nexen under the Sales Agreement; (3) maintain records of quantities and total heating value of gas sold by Nexen and transportation volumes allocated at the Niagara check meter by TGP; (4) analyze and reconcile the nominated and received gas volumes; (5) coordinate re-offerings of gas not nominated by Berkshire to other companies in the Working Group; (6) notify Berkshire of the effective monthly contract price and, when applicable, the effective reference price under the Sales Agreement; (7) coordinate meetings of the Working Group, Nexen and TGP, and any other appropriate parties, as may be necessary to discuss and resolve operational, commercial, and regulatory issues; and (8) remit sums due and owing by Berkshire to Nexen and third parties

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[6] The other members of the Working Group also are parties to the Management Services Agreement, receiving the same services from NEGM for their respective sales agreements (Exh. BG-4, at 1).

under the Sales, Agency, and Management Services Agreements (Exhs. BG-1, at 15-16; BG-4, at 3-4).

The Management Services Agreement is conterminous with the Sales Agreement (Exh. BG-4, at 8-9). However, Berkshire has the right to terminate the Management Services Agreement under specified conditions (id. at 9). The Management Services Agreement can also be renewed (id.).

D. The Request For Proposals Process

1. Sales Agreement

The Working Group issued a joint request for proposals ("RFP") for a replacement gas supply to 22 potential bidders[7] on August 14, 2003 (Exhs. BG-1, at 7; BG-7, at 1). The estimated total replacement volumes were approximately 120,000 Dth per day (Exh. BG-1, at 7). The Working Group encouraged bids with a range of volume options that would provide delivery flexibility; bids with multiple terms and pricing options; bids based on a 100 percent take, or base load; and bids that included first-of-the-month flexibility (id. at 8-9). The Working Group gave bidders the opportunity to ask questions or seek clarification of the RFP's objectives (id. at 8). The deadline for the submission of bids was September 5, 2003

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7 The proposed RFP recipients for EnCana gas replacement supplies were: Amerada Hess Corp., Apache Canada Ltd., BP Canada Energy Company, Canadian Natural Resources Ltd, Cargill, Cinergy, Constellation Power, Coral Energy, DTE Energy, Duke Energy Trading and Marketing, Emera, EnCana Corporation, Husky, Imperial Oil, Marathon Canada, NRJ Energy, Nexen, Proliance Energy, RWE Trading Americas, Sempra Energy Trading, Sprauge, and Tenaska (Exh. BG-9).

(Exh. BG-7, at 6). At the close of the solicitation process, twelve suppliers[8] submitted bids and ten suppliers elected not to participate in the RFP process (Exh. BG-1, at 8).

Berkshire states that the Working Group determined that Nexen and BP Canada Energy Company ("BP") were essentially equivalent and represented the best price and overall value (id. at 11). Berkshire maintains that it elected to negotiate a gas sales agreement with Nexen primarily to add a measure of diversity to its resource portfolio, as Berkshire secures a substantial portion of its pipeline volumes from an affiliate of BP pursuant to a supply contract approved in The Berkshire Gas Company, D.T.E. 02-81 (2003) (id.).

2. Agency and Management Services Agreements

Berkshire did not conduct a separate solicitation to receive proposals to provide agency and management services before entering into agreements with NEGM (id. at 16.) According to the Company, the costs associated with conducting an RFP outweighed the existing costs it currently paid NEGM for services (id.). Berkshire concludes that the potential benefits from any solicitation would be dramatically less than the costs of such process (id. at 17). Berkshire states that it monitored KeySpan Energy Delivery New England's ("KeySpan") RFP process before making a final decision on selecting an agent (KeySpan is a member of the Working Group, see n. 3 above) (id.).[9] Berkshire notes the high level of performance it has received

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8 Amerada Hess Corp, BP Canada Energy Company, Canadian Natural Resources Ltd, Cargill, Coral Energy, DTE Energy, Emera, Husky, NRJ Energy, Nexen, Sempra Energy Trading, and Sprague submitted bids (Exh. BG-10).

9 For a discussion of KeySpan's RFP process for its agency and management services agreements see KeySpan Energy Delivery New England, D.T.E. 04-29 (2004).

from NEGM through its previous agreements, and NEGM's willingness to negotiate a reduction in its charges (id.).

III. STANDARD OF REVIEW

In evaluating a gas utility's resource options for the acquisition of commodity resources as well as for the acquisition of capacity under G.L. c. 164, § 94A ("Section 94A"), the Department examines whether the acquisition of the resource is consistent with the public interest. Commonwealth Gas Company, D.P.U. 94-174-A at 27 (1996). In order to demonstrate that the proposed acquisition of a resource that provides commodity and/or incremental resources is consistent with the public interest, an LDC must show that the acquisition (1) is consistent with the company's portfolio objectives and (2) compares favorably to the range of alternative options reasonably available to the company and its customers, including releasing capacity to customers migrating to transportation, at the time of the acquisition or contract negotiation. Id.

In establishing that a resource is consistent with the company's portfolio objectives, the company may refer to portfolio objectives established in a recently approved forecast and requirements plan or in a recent review of supply contracts under Section 94A, or may describe its objectives in the filing accompanying the proposed resource. Id. In comparing the proposed resource acquisition to current market offerings, the Department examines relevant price and non-price attributes of each contract to ensure a contribution to the strength of the overall supply portfolio. Id. at 28. As part of the review of relevant price and non-price attributes, the Department considers whether the pricing terms are competitive with those for the broad range of capacity, storage, and commodity options that were available to the LDC at the time of the acquisition, as well as those opportunities that were available to other LDCs in the region. Id. In addition, the Department determines whether the acquisition satisfies the LDC's non-price objectives, including, but not limited to, flexibility of nominations and reliability and diversity of supplies. Id. at 29. In making these determinations, the Department considers whether the LDC used a competitive solicitation process that was fair, open and transparent. The Berkshire Gas Company, D.T.E. 02-56, at 9; Bay State Gas Company, D.T.E. 02-52, at 8 (2002); KeySpan Energy Delivery New England , D.T.E. 02-54, at 9 (2002); The Berkshire Gas Company, D.T.E. 02-19, at 11 (2002).

IV. ANALYSIS AND FINDINGS

A. The Request For Proposal Process

1. Sales Agreement Request for Proposal

The bid solicitation and evaluation process followed by Berkshire and the Working Group for procurement of gas supplies in this proceeding was similar to the process approved in recent proceedings. D.T.E. 02-56, at 9; D.T.E. 02-52, at 8; D.T.E. 02-54, at 9; D.T.E. 02-19, at 11. In determining whether the RFP process was fair, open, and transparent, the Department notes that potential bidders were notified on the specifics of how each bid would be evaluated (Exh. BG-8). Specifically, the evaluation process was clearly stated to each potential bidder, evaluation criteria were provided, and there was an opportunity for bidders to request clarification from the Working Group on both the evaluation criteria and the RFP process itself (id.). In addition, the bids were evaluated and the winning bid was selected based on the criteria set forth in the RFP (Exh. BG-1, at 10). Furthermore, the Company received no objections from potential bidders to indicate that a bidder was unfairly excluded from initial consideration or that a bid was unfairly evaluated (id.). Finally, our review of the responses to the RFP indicates that the Company's proposal compares favorably to current market offerings considering price and non-price factors, as well as current market conditions facing the Company at the time of the execution of the Agreement. Accordingly, the Department finds that the RFP process conducted by the Working Group and followed by Berkshire for the procurement of gas supplies was transparent, fair and open.

2. Agency and Management Services Agreements Request for Proposal

In D.T.E. 02-56, the Department directed Berkshire to conduct an RFP to test the market for alternative offerings available to it before renewing the current agency and management services agreements with NEGM or, alternatively, to provide evidence to show that there is no other entity that is capable of providing similar services as NEGM. Id. at 12. Berkshire did not comply with this Department directive. Berkshire did not issue its own RFP for agency and management services. Berkshire did not inform the Department that it would not issue an RFP or, in advance of this filing, explain to the Department that complying with the Department's directive would not be cost effective, and did not otherwise seek relief from the requirements of D.T.E. 02-56 (Tr. at 10). Rather, Berkshire relied on the results of KeySpan's separate solicitation of agency and management services (Exhs. BG-1, at 16; DTE 1-5; DTE 1-15; RR-DTE-1).

The purpose of the Department's directive in D.T.E. 02-56 regarding the RFP process was to ensure that Berkshire's customers receive the maximum benefit from the activities of the Company. The record shows that Berkshire was fully aware of the Department's directive (Exhs. BG-1, at 16-17; DTE 1-5; DTE 1-15; RR-DTE-1). Although Berkshire claimed that the cost of conducting an RFP would be prohibitive, Berkshire provided no cost data or any supporting analysis (id.). Furthermore, although Berkshire relied on KeySpan's RFP for management services, there is no evidence that the Company participated directly in that process or provided KeySpan with any input on its RFP process.

Prior to acquiring commodity and/or capacity resources and ancillary services, an LDC is expected to test the market to ensure that the terms of the contract(s) are competitive with those available at the time of the acquisition, as well as with opportunities available to other LDCs in the region. See D.T.E. 94-174-A at 28. This form of testing can be conducted in many ways, including informal and formal solicitations from entities providing the service that the LDC wishes to procure. While we are aware of the opportunities available to KeySpan,[10] we have no evidence in this case on the options available to Berkshire pertaining to agency and management services.

The duty to issue an RFP or to provide evidence that no other entity is capable of provide these services, as directed by the Department, runs directly to the Company. Unless the Department sanctions such a course, the Company cannot satisfy this duty merely by monitoring and relying on the actions of another LDC. The Department is open to evaluating its directives and the resulting duties imposed where a company presents information on a

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10 KeySpan Energy Delivery New England, D.T.E. 04-29 (2004).

change in circumstances, or on an alternative method, or that complying with the directive would not be cost effective. In this case, Berkshire failed to take any of these steps. As a result of the Company's failure to comply with the Department's directive, we cannot determine whether NEGM is the best option for providing agency and management services to the Company

B. Sales Agreement

The Department's review of Berkshire's proposal indicates that the Sales Agreement is consistent with the Company's resource portfolio objectives established in the Company's most recent forecast and requirements plan in The Berkshire Gas Company, D.T.E. 02-17 (2003) . Under the proposed Sales Agreement, Nexen will provide Berkshire with 1,080 Dth per day, on a firm basis, to replace the EnCana contract volumes (Exh. BG-1, at 13). The replacement resource will enable the Company to continue to provide reliable service to its customers (id.).

The Department finds that the competitive solicitation process which led to the selection of Nexen as the winning bid ensured that Berkshire obtained a least-cost resource consistent with its portfolio objectives. The Nexen resource compares favorably to the range of alternatives reasonably available to the Company and its customers at the time of the agreements and enhances the diversity of the Company's resource portfolio. Furthermore, we find that Berkshire's participation in the Working Group ensured that the Company enjoyed substantial economies of scale in securing a least-cost replacement resource.

The Department finds that, as a replacement resource, the Sales Agreement is consistent with the Company's resource portfolio objectives and compares favorably to the range of alternatives reasonably available to the Company and its customers at the time of the agreement. Accordingly, the Department finds that the Sales Agreement is consistent with the public interest, and we approve the Company's proposal.

C. Agency and Management Services Agreement

We conclude that the services to be performed under the Agency and Management Services Agreement are necessary and consistent with Berkshire's portfolio objectives established in the Company's forecast and requirements plan in D.T.E. 02-17 (2003). NEGM has a long-working relationship with the Working Group dating back over 20 years, and NEGM has substantial Canadian gas contracting expertise (Exh. BG-1, at 16). Furthermore, the services that NEGM will provide under these agreements are a continuation of the services that NEGM currently provides under the EnCana agreements. D.T.E. 02-56, at 4-5. Under the Management Services Agreement, NEGM will provide the same services at a lower rate than it charged under the EnCana agreements (Exh. BG-1, at 17). Therefore, the Department finds that the Company's ratepayers will likely benefit through lower costs compared to the current arrangement, as a result of the experience and expertise of NEGM. For these reasons, the Department finds that the Agency and Management Services Agreements are consistent with the public interest and the Department approves these agreements.

However, a question is raised regarding the prudence of Berkshire's actions in procuring NEGM's services. The record shows that Berkshire elected generally to observe and rely on the results of KeySpan's solicitation rather than perform its duty as directed by the Department. Companies are not free to disregard a Department directive without consequence.

Thus, companies under the jurisdiction of the Department are on notice that failure to comply with a Department directive will be at risk of disallowance of costs associated with the duty imposed by the Department's directive.

At this time, the Department does not rule on the propriety of Berkshire's rate recovery of the compensation to be paid under the Agency and Management Services Agreement. The Department will consider this issue of cost recovery in the Company's next scheduled gas adjustment factor ("GAF") filing with the Department. The burden will be on Berkshire in that next scheduled GAF filing to justify recovery of the compensation paid to NEGM under the Agency and Management Services Agreements. Accordingly, we direct the Company to provide in that filing (i) cost data regarding the Company's potential use of a competitive solicitation for the procurement of agency and management services, (ii) documentation of the Company's decision making in forgoing the use of a competitive solicitation process, (iii) documentation of Berkshire's communications with KeySpan and its involvement in KeySpan's process for soliciting agency and management services, and (iv) other information the Company deems appropriate to support the recovery of the costs paid for agency and management services from NEGM. What is sought is clear evidence of actions and documentation that predates the decision to enter into the Agency and Management Services Agreements, for that would be more persuasive than after-the-fact opinion testimony.

Furthermore, the Department directs Berkshire for its next filing pertaining to approval of an agency and/or management services agreement either to: (a) conduct an RFP for agency and management services or provide other proof that the Company tested the market; or

(b) provide justification with supporting documentation, calculations, and other relevant information to support any assertion that issuing an RFP or testing the market would be not be cost effective.

V. ORDER

Accordingly, after due notice, hearing, and consideration, it is hereby

ORDERED: That the gas sales agreement with Nexen Marketing and The Berkshire Gas Company is hereby APPROVED; and it is

FURTHER ORDERED: That the agency agreement between Northeast Gas Markets LLC and The Berkshire Gas Company is hereby APPROVED subject to the Department's review of the associated cost recovery in the Company's next scheduled gas adjustment factor filing under 220 C.M.R. §§ 6.00 et seq.; and it is

FURTHER ORDERED: That the management services agreement between Northeast Gas Markets LLC and The Berkshire Gas Company is hereby APPROVED subject to the Department's review of the associated cost recovery in the Company's next scheduled gas adjustment factor under 220 C.M.R. §§ 6.00 et seq.; and it is

FURTHER ORDERED: That the Berkshire Gas Company shall follow all other directives contained in this Order.

By Order of the Department,

/s/______________________________
Paul G. Afonso, Chairman

/s/________________________________
James Connelly, Commissioner

/s/______________________________
W. Robert Keating, Commissioner

/s/_______________________________
Eugene J. Sullivan, Jr., Commissioner

/s/________________________________
Deirdre K. Manning, Commissioner

Appeal as to matters of law from any final decision, order or ruling of the Commission may be taken to the Supreme Judicial Court by an aggrieved party in interest by the filing of a written petition praying that the Order of the Commission be modified or set aside in whole or in part.

Such petition for appeal shall be filed with the Secretary of the Commission within twenty days after the date of service of the decision, order or ruling of the Commission, or within such time as the Commission may allow upon request filed prior to the expiration of twenty days after the date of service of said decision, order or ruling. Within ten days after such petition has been filed, the appealing party shall enter the appeal in the Supreme Judicial Court sitting in Suffolk County by filing a copy thereof with the Clerk of said Court. (Sec. 5, Chapter 25, G.L. Ter. Ed., as most recently amended by Chapter 485 of the Act of 1971).